AMOCO PRODUCTION COMPANY

IBLA 71-306 Decided April 3, 1973

Appeal from a decision of the Director, Geological Survey, assessing $16,400 in additional royalties for gas production allocated to oil and gas leases Cheyenne 048240 and Cheyenne 048242.

Affirmed.

Contracts: Construction and Operation: General Rules of Construction

Government oil and gas leases, as well as unitization agreements requiring governmental approval, are subject to the same rules of construction as those applied in interpreting a contract between two private parties.

Contracts: Construction and Operation: Generally

Where a section of a unitization agreement is unambiguous and only one interpretation thereof may properly be made consistent with the language, the doctrine of practical construction will not be followed and the plain meaning will control.

APPEARANCES: T. J. Files, Esq., and Louis C. Ross, Esq., for the appellant.

OPINION BY MR. HENRIQUES

Amoco Production Company appeals from a decision of the Director, Geological Survey, dated January 6, 1971, assessing $16,400 in additional royalties on gas produced from the participating areas established for the Frontier and Dakota formations under the Beaver Creek Unit Agreement and allocated to leases Cheyenne 048240 and Cheyenne 048242.

The basic issue on appeal is the proper interpretation of the Beaver Creek Unit Agreement entered into on March 29, 1937, as that agreement relates to the computation of royalties. The unit agreement was approved by the Acting Secretary of the Department of the Interior on August 6, 1937. The Acting Secretary further provided that "each and every lease heretofore or hereafter issued for a period of 20 years for lands of the United States subject to said agreement

* * * shall be modified to conform with this agreement * * *" 1/ The lease provisions for Cheyenne 048240 and Cheyenne 048242, entered into on February 8, 1939, by appellant's predecessor in interest, provided in relevant part for royalty payments:

> On gas, whether same shall be gas from which the casing-head gasoline has been extracted or otherwise, 12-1/2 per cent of the value thereof in the field where produced where the average production per day for the calendar month from the land leased is less than 3,000,000 cubic feet, and 16-2/3 per cent where the average daily production is 3,000,000 cubic feet or over. (Emphasis supplied)

The Beaver Creek Unit Agreement in section 10(b) provided as follows:

> That royalty to the United States shall be paid at the rate specified in the respective Federal permits or leases based on the amount of production allocated to the tracts thereof; provided that, for leases which the royalty rate on oil depends on the average daily oil production per well, the royalty rate in each participating area shall be determined for each lease by the average daily production of the oil wells subject to this agreement producing from that participating area; and for leases for which the royalty rate on gas depends on the average daily gas production per well, the royalty rate in each participating area shall be determined for each lease by the average daily production of gas per well subject to this agreement producing from that participating area. (Emphasis supplied)

The problem presented by this case is that while the lease terms provided that the royalty rate for oil was to be determined by the average daily production per well, the lease terms further provided that the royalty rate for gas was to be determined by the average daily production "from the land leased." Appellant contends that

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1/ This declaration merely restated part of § 17 of the unit agreement which declared that:
"The terms, conditions, and requirements of each and every permit, lease, operating agreement, or other instrument subject to and/or by reference made a part of this contract be and hereby are amended, modified and extended in conformity with the terms and provisions of this contract, and compliance with the requirements of this contract shall be and constitute compliance with all the terms, conditions, and requirements of each and every permit, lease, and operating agreement or other instrument subject to and/or by reference made a part of this contract as aforesaid."

the royalty rate is, therefore, governed by the opening clause of section 10(b), viz, "[t]hat royalty to the United States shall be paid at the rates specified in the respective Federal permits or leases based on the amount of production allocated to the tracts thereof * * *." From this it argues that the term "tracts" means "those portions of lands out of each lease placed in a participating area according to the allocation formula for participation as it is set out in the first part of [§10]."

A number of different participating areas were established, among which were the Madison, Frontier and Dakota formations. The practical effect of appellant's interpretation of the unit agreement was that the sliding scale rate would not be triggered until allocated production from a single formation (i.e., participating area) exceeded 3,000 MCF. 2/ Such occurred only in the Frontier formation at which time appellant paid the increased royalty rate.

Appellant's interpretation of the unit agreement was accepted as correct until February 2, 1967, when the Casper, Wyoming, office of the Geological Survey made demand for $14,225.07 in unpaid royalties. The Geological Survey took the position that that portion of section 10(b) which reads "* * * royalty to the United States shall be * * * based on the amounts allocated to the tracts thereof," merely permitted the determination of the royalty due on the basis of constructive production in lieu of actual production, and did not vary the requirement that royalties be paid on gas produced "from the land leased" as a single entity. Thus, allocated production, the Geological Survey contended, must be totaled from all productive horizons to determine the royalty rate and, hence, the amount of royalty due.

On August 7, 1968, the Regional Oil and Gas Supervisor, Casper, Wyoming, made demand for payment of more than $16,400 in additional royalties. Amoco appealed to the Director of the Geological Survey. The Director, on January 6, 1971, denied the appeal. In his decision the Director adopted the view that the only effect of the phrase "allocated to the tracts" was to allow constructive production. The Director cited Sinclair Oil and Gas Company, 75 I.D. 155 (1968), to the effect that the action by the Geological Survey in accepting the lesser payments tendered by the appellant was an error, the type of which had been held not to estop the United States, and indeed that the Geological Survey was without authority to accept less than the royalty called for in the lease.

2/ The last sentence of § 9 provides that: "Separate participating areas may be designated for separate productive horizons."

While we agree that the Geological Survey is obligated to accept only full payment of the required rental, we believe its reliance on Sinclair Oil and Gas Company, supra, is, in one sense, misplaced. Sinclair involved the interpretation of section 12 of the Act of August 8, 1946, 30 U.S.C. § 226(c) (1970). As that opinion expressly noted:

> The general rule is, of course, well established that neither the unauthorized acts of government employees nor their laches can effect the rights of the United States or confer upon any individual or entity a right not authorized by law. * * * On the other hand, the acts or omissions of officers of the Government, if they be authorized to bind the United States in a particular transaction, will work estoppel against the Government if the officers have acted within the scope of their authority. * * * (Citations omitted) Sinclair Oil and Gas Company, supra, at 169.

There is no statute prohibiting the fixing of royalty rates for gas on the basis of allocated production to participating areas, if the Government so desires. The question for decision is whether such was the intent of the parties. If such was the intent of both parties, the issue of estoppel is not presented. Only if the parties intended royalty payments to be computed on the basis of all production allocated to the leased land, would the issue of estoppel be properly considered.

Initially, it should be noted that both the lease and the unit agreement are subject to the general rules of contract construction. See Reading Steel Casing Company v. United States, 268 U.S. 186, 188 (1925). Appellant strenuously contends that the subsequent action of the parties have evinced an agreement as to the proper interpretation of the unitization agreement. It has been noted that "[w]here parties have accorded a practical construction to their contract '* * * this construction will be given substantial weight in determining the proper interpretation, particularly if the conduct manifesting their construction occurred prior to any controversy.'" Boswell v. Chapel, 298 F.2d 502, 506 (10th Cir. 1961) citing Fanderlik-Locke Co., v. United States, 285 F.2d 939, 947 (10th Cir. 1960), cert. denied 365 U.S. 860.

This doctrine, however, is not without exceptions. In Portsmouth Baseball Corp. v. Frick, 278 F.2d 395 (2d Cir. 1960), the Court noted that: "[b]ecause Major-Minor League Rule 1(a) is clear and unambiguous, it cannot be stretched by resorting to an interpretation allegedly resulting from the subsequent conduct of the parties. Where,

as here, the contract is plain and definite, the doctrine of practical construction does not apply." Id. at 400 (Citations omitted). See also, 4 Williston on Contracts § 623 at 792: "But whatever the nature of the case the court will apply the canons of contemporaneous and subsequent construction unless this is contrary to the plain meaning of the contract." (Emphasis supplied)

The lease agreement clearly states that the royalty rate for gas production is to be based on the amount of production from "the land leased." The unit agreement declares "[t]hat royalty to the United States shall be paid at the rates specified in the respective Federal permits or leases based on the amount of production allocated to the tracts thereof * * *." (Emphasis supplied) The proviso following this section contains two instances in which the lease would be modified, neither of which is applicable here. Applying the doctrine of expressio unius est exclusio alterius it is apparent that the lease term calling for the payment of the royalties "from the land leased" was not intended to be modified by the unit agreement insofar as it related to gas production. If allocation "to the tracts thereof" was read, as Amoco contends it should be, as allocation "to the productive horizon of each participating area" the proviso, itself, becomes superfluous since such a reading would effectively accomplish for oil production royalty computed on the basis of average daily production per well, exactly what the proviso specifies. As the purpose of a proviso is to qualify the general statements preceding it, see Ernest Alpers, A-30627 (March 10, 1967), appellant's interpretation of the phrase "allocated to the tracts thereof * * *" can only be seen as both strained and unrealistic. Since the plain meaning of the lease terms, read in conjunction with the unit agreement, conclusively show that the royalty rate for gas production was not to be varied from the rates specified in the lease, the doctrine of practical construction is nonapplicable.

Furthermore, there is no evidence of any Government concurrence in the method of Amoco's computation of royalty rates as such method relates to the interpretation of the lease and unit agreement. All that the record before us indicates is that Amoco's payments were accepted when tendered. There is no statement by any agent of the Government, authorized or unauthorized, to the effect that the computation of royalties on the basis of productive horizons of participating areas was proper. There is merely the silent acquiescence of Government employees in receiving Amoco's royalty payments. Such passive acceptance does not rise to the level of a mutual construction, and thus, for an additional reason the doctrine of practical construction does not apply.

Having determined that the clear meaning of the documents involved herein requires royalty payments to be computed on the

basis of all production allocated to the leased land, the issue of estoppel must be considered. Here, we think that the Geological Survey's reliance on Sinclair Oil and Gas Company, supra, is more on point. We note that the Department's decision in Sinclair holding that the Government could not be estopped by past actions from receiving the full amount of royalty required was affirmed by the United States District Court, sub nom. Atlantic Richfield Co. v. Hickel, 303 F. Supp. 724 (D. Wyoming 1969), and by the Tenth Circuit Court of Appeals, 432 F.2d 587 (1970). See also Brandt v. Hickel, 427 F.2d 53 (9th Cir. 1970); Gestuvo v. District Director of U.S. Imm. & Nat. Svc., 337 F. Supp. 1093 (C. D. Cal. 1971); and, as to leases, Tenneco Oil Co., 8 IBLA 282 (1972); Mark Systems, Inc., 5 IBLA 257 (1972). Thus, the determination of the Geological Survey was correct and will not be disturbed.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

Douglas E. Henriques, Member

We concur:

Martin Ritvo, Member

Joseph W. Goss, Member.